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BUMPER 2019 FOR GLOBAL MARKETS - WHERE TO FOR 2020?

By Brian Butchart, Managing Director and Key Individual, Brenthurst Wealth Management

The Brenthurst Global Equity and Brenthurst Global Balanced Fund delivered stellar USD returns, up 26% and 18% respectively over the last 12 months, while other international funds selected in our global portfolios delivered in excess of 30%.

International markets had a bumper year in 2019! The MSCI All-World index continued to rise by over a quarter, it's best performance since 2009. The S&P 500 was up 30%, the NASDAQ by 35% and the Euro Stoxx 50 by 25%. After a poor 2018, China's CSI 300 index rebounded, rising by a third during the year.

Despite continued geopolitical risks such as Brexit and the US-China trade wars, international markets delivered double digit returns in hard currency.

For almost a decade, Brenthurst Wealth has been advising clients to invest a portion of their assets globally, beyond the borders of South Africa for several reasons:

- ① **DIVERSIFICATION:** As the JSE ALSI represents less than 1% of global investment opportunities, investors who restrict their opportunity set to domestic assets miss out on more than 99% of available investment opportunities presented by listed assets around the globe.

Investing abroad provides access to industries currently not available in South Africa (eg: information technology, biotechnology, electronics and pharmaceuticals to name a few).

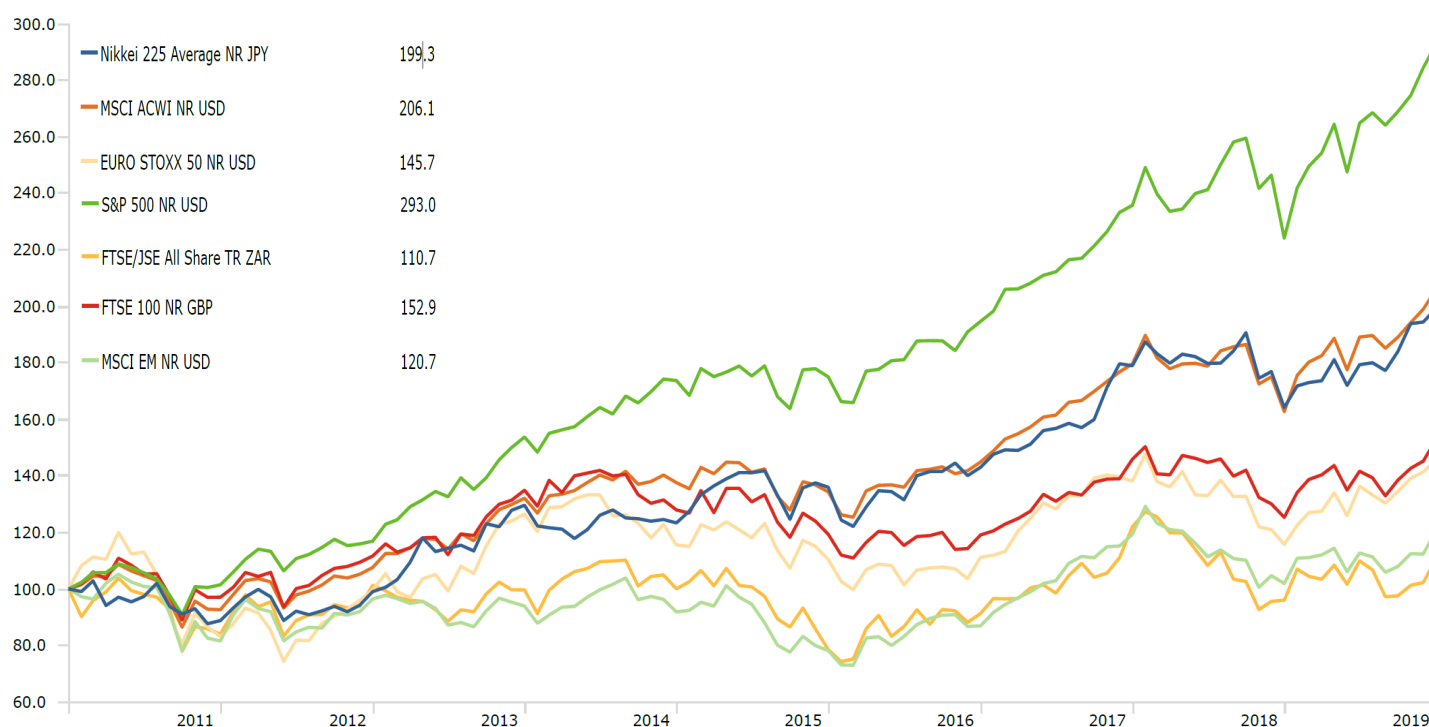
In addition to a much wider opportunity set, our preferred global equity benchmark, the MSCI All Country World Index, currently comprises of more than 2 500 investable companies compared to roughly 100 that drive the returns of the local market.

Diversifying internationally allows for investor-participation in growth regions benefitting from mega-drivers such as industrialisation, urbanisation, digital advances and growing consumerism.

ALL MARKETS, INCLUDING EMERGING MARKETS, DELIVERED STRONG USD RETURNS IN 2019. OVER 1, 3, 5 AND 10 YEARS ALMOST ALL INTERNATIONAL MARKETS HAVE LEFT SA TRAILING IN BOTH US DOLLARS AND RANDS AS CAN BE SEEN IN THE FOLLOWING CHARTS AND TABLES.

10 YEARS GROWTH - USD

TIME PERIOD: 12/31/2010 TO 12/31/2019



ANNUALISED USD RETURNS

Data Point: Return Currency: US Dollar

	1 Year	3 Years	5 Years	10 Years
Nikkei 225	21.35	11.69	10.07	8.47
S&P 500 USD	30.70	14.59	11.01	12.85
FTSE 100 GBP	21.99	8.68	3.62	
MSCI ACWI USD	26.60	12.44	8.41	8.79
FTSE/JSE All Share TR ZAR	15.26	6.63	2.04	3.90
MSCI EM USD	18.42	11.57	5.61	3.68
EURO STOXX 50 USD	25.89	9.42	4.74	2.85

② OPTIMISATION: Studies on optimal SA portfolios normally recommend a minimum offshore allocation of 20% to 30% through the cycle for long-term investors requiring a return of inflation plus 4% to 5% in rand terms.

This is a classic recommendation for retirement savers aiming to optimise outcomes for their future pension, restricted by regulation 28 of the Pension Act. Investors with more global spending requirements, including a larger share of foreign currency denominated spending, or where multiple generations may live on different continents, can typically justify a larger offshore allocation.

Whatever strategic allocation range an investor deems to be appropriate, Brenthurst Wealth believes investors should still have an offshore allocation at the higher end of their appropriate strategic weighting, given the elevated level of economic and political risks facing South Africa at present.

③ PROTECTION AGAINST DECLINING PURCHASING POWER due to the devaluation of the local currency over time. The Rand is one of the most volatile emerging market currencies in the world and one of the main reasons foreign investment should be considered as a long-term investment.

Many items in a consumer's shopping basket, from fuel to food to healthcare, are largely priced in foreign currencies as the inputs are either commodities with prices struck in global markets, or heavily reliant on imported content. Viewed from this perspective, having adequate offshore exposure is merely a hedge against the long-term change in price of this part of your future shopping basket. Episodes of currency weakness will more than likely remain a strong driver of price increases into the future.

It is widely expected that the Rand will continue to gradually weaken against all major international currencies as has been experienced for several decades.

THE RAND OVER THE LAST 20 YEARS DEPRECIATED AGAINST THE DOLLAR ON AVERAGE BY 4.24% PER ANNUM, WITH THIS LONGER-TERM TREND EXPECTED TO CONTINUE.

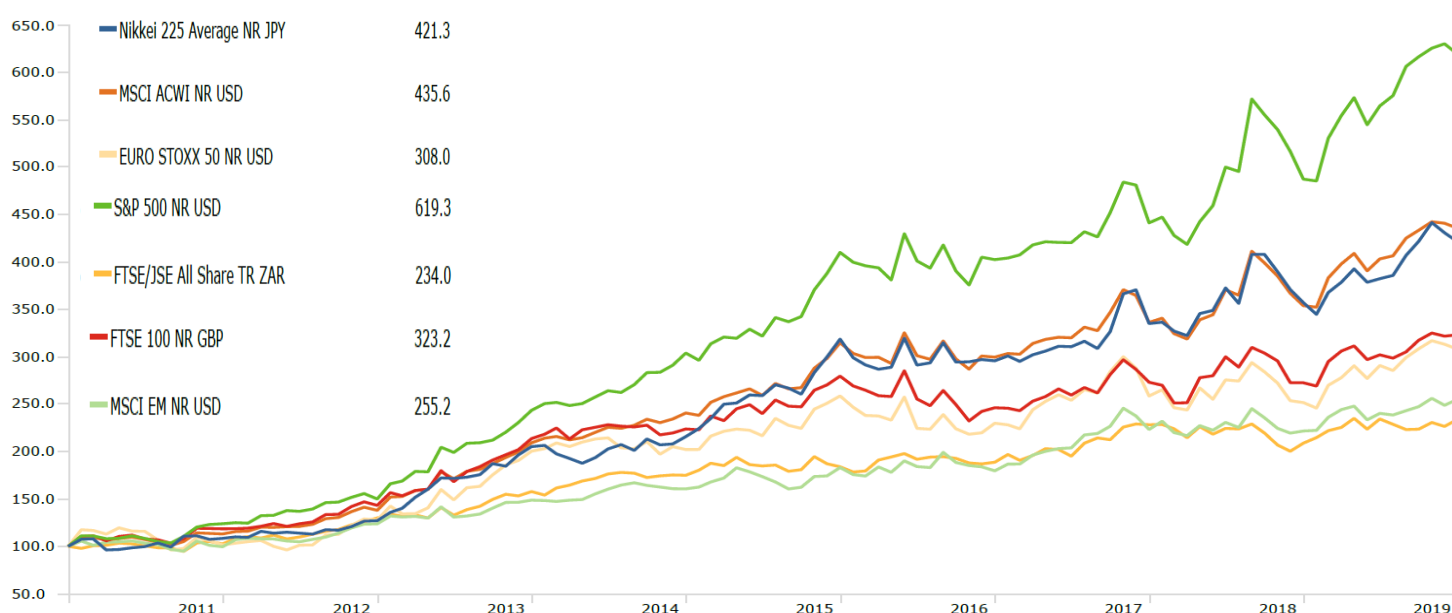


④ LACK OF STRUCTURAL REFORM AND POLITICAL WILL. Over several years Brenthurst reported on the political uncertainty, corruption and lack of reform hindering the SA economy. This is not being negative or unpatriotic, but simply reporting facts to enable informed investment advice and decisions.

Of course, we are hopeful of a recovery and although possible, unlikely immediately, considering the magnitude of South Africa's woes. The economy is faltering, unemployment worsening, load shedding is expected to remain a regular feature while SOE's are bankrupt. State spending remains unabated, municipalities are teetering on the brink of collapse and there is no decisive measures to stop the deterioration of government finances. Unfortunately, the hope instilled in Cyril Ramaphosa's cabinet has waned. The more time passes without definitive action, the less confidence this creates, and the impact on the local stock market and rand evident for several years now. See below the performance of the JSE relative to global markets in local currency.

10 YEARS GROWTH CHART - ZAR

TIME PERIOD: 12/31/2010 TO 12/31/2019



ANNUALISED ZAR RETURNS

Data Point: Currency: South African Rand

	1 Year	3 Years	5 Years	10 Years
Nikkei 225	17.97	12.52	14.32	15.65
S&P 500 USD	27.05	15.44	15.30	20.33
FTSE 100 GBP	18.58	9.49	7.63	
MSCI ACWI USD	23.06	13.28	12.60	15.99
FTSE/JSE All Share TR ZAR	12.05	7.42	5.99	10.78
MSCI EM USD	15.12	12.40	9.69	10.54
EURO STOXX 50 USD	22.37	10.24	8.78	9.66

Our bias towards international assets delivered strong double digit, inflation beating returns for clients in dollars and Rand's beating the dismal performance offered by the local market which has been under pressure for more than 7 years now, barely beating inflation.

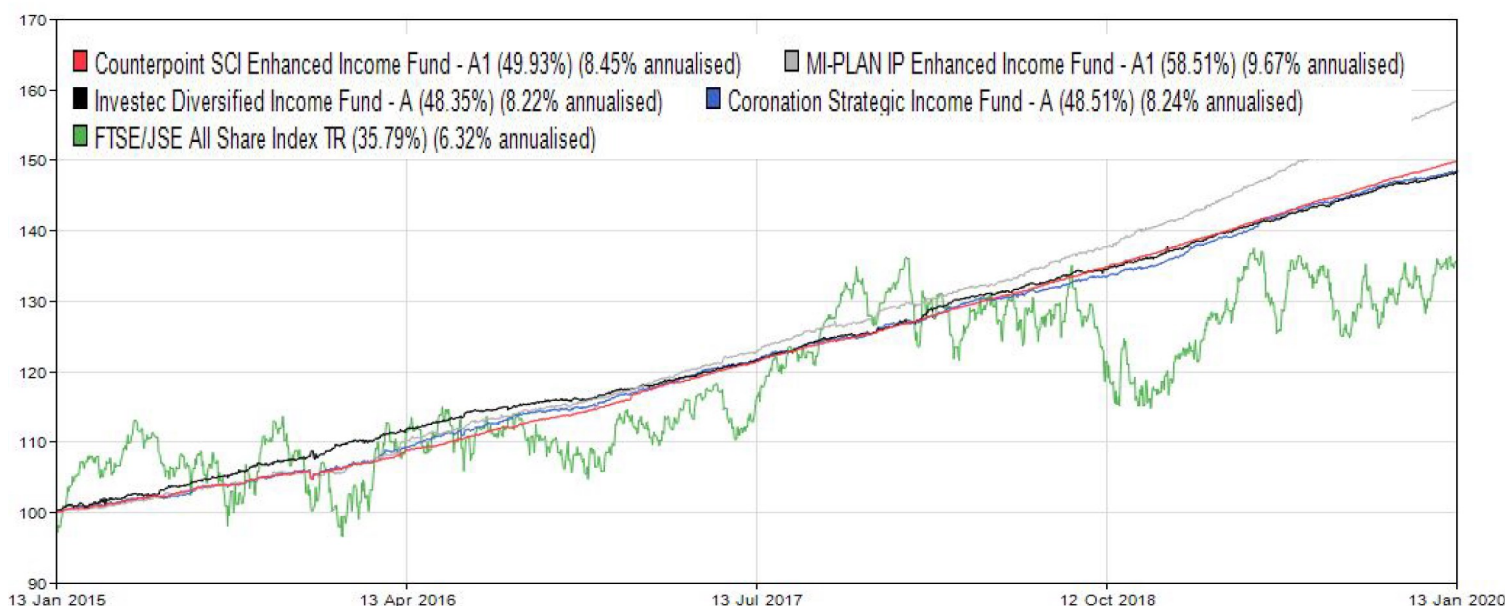
Besides a longer-term offshore strategy, Brenthurst employed an alternative local strategy for assets that may have been restricted to SA, such as pension, provident and retirement annuity funds and/or clients requiring a more conservative investment solution.

In order to counter the impact of the poor performance from the local market, Brenthurst implemented a change in strategy across regulation 28 funds by reducing local equity exposure and increasing exposure to local cash and bonds (income funds), in some cases increasing allocation to local income funds up to 70% with the remaining 30% allocation invested offshore (within regulation 28 requirements).

The income funds we've been using are the Mi-Plan Enhanced Income, Counterpoint Enhanced Income, Coronation Strategic Income and Investec Diversified Income funds with ALL beating the JSE ALSI over 1, 3 and 5 years at substantially less risk.

ANNUALISED RETURNS OVER 5 YEARS

TIME PERIOD: 13 JANUARY 2015 TO 13 JANUARY 2020



PERFORMANCE SUMMARY TABLE

Fund	1 Month (%)	3 Month (%)	1 Year (%)	3 Year (%)	3 Year annualised (%)	5 Year (%)	5 Year annualised (%)
Counterpoint SCI Enhanced Income Fund - A1	0.64	1.89	8.79	29.60	9.04	49.93	8.45
MI-PLAN IP Enhanced Income Fund - A1	0.84	2.37	11.99	35.52	10.68	58.51	9.67
Investec Diversified Income Fund - A	0.58	1.44	7.95	26.31	8.11	48.35	8.22
Coronation Strategic Income Fund - A	0.50	1.30	8.96	27.33	8.40	48.51	8.24
FTSE/JSE All Share Index TR	1.54	3.99	11.03	19.91	6.25	35.79	6.32

Data as at 13 January 2020
Including reinvestments

EXPECTATIONS FOR 2020

- ⇒ The World Bank recently cut growth forecasts to below 1% for SA, largely due to the highly detrimental impact of continued load shedding on the economy.
- ⇒ Stage 2 load shedding resurfaced early in 2020, well before most businesses and industries are in full operation, expected to worsen as demand for electricity increases as companies reopen.
- ⇒ Persistent uncertainty and more aggressive load shedding levels will impact foreign direct investment, political and economic stability, employment and economic growth.
- ⇒ An unreliable power supply, places an enormous amount of constraint on the South African economy and will continue to deter local and foreign investment, urgently required to alleviate unprecedented unemployment and reignite growth.

Economist Mike Schussler reported about the magnitude of the South African challenges equities have endured, compared to other emerging market peers:

Another decoupling: SA and Emerging Markets - Equity Indices decoupled slowly at 1st but since the firing of Nene big time. If SA stayed with EM indices the JSE would have been valued about R2,5 trillion higher now. Our Pensions, investors etc suffered. savings destruction!

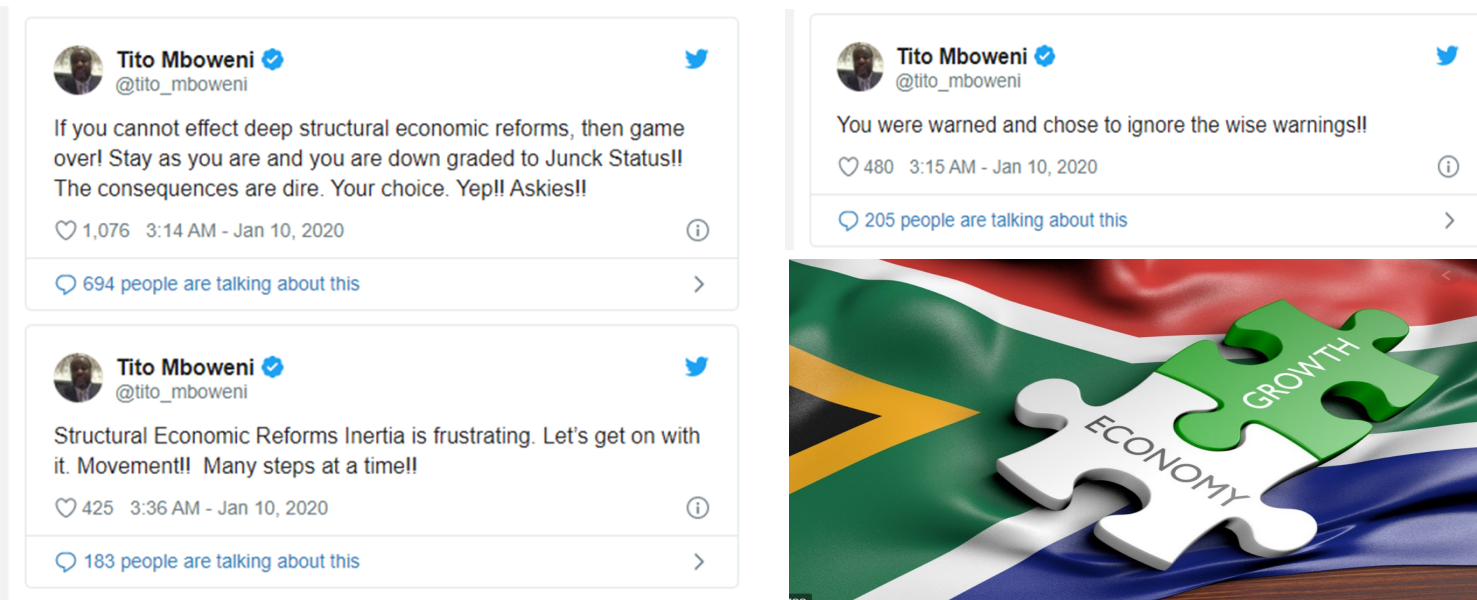
SA AND EMERGING MARKET EQUITIES ALSO DECOUPLED AFTER MINISTER NENE WAS FIRED



- ⇒ Although the JSE may be cheap based on historical valuations, it could remain subdued for longer on the back of lower expected earnings, considering the uncertainties regarding Eskom and the impact on growth and the economy.
- ⇒ Investors seeking insights on the outlook for the JSE ALSI that failed to keep pace with emerging market peers over the last 7 years and barely beating inflation are waiting to see how the ruling party addresses the first key event this quarter – The Budget and Eskom. With the World Bank lowering South Africa's growth forecast below 1%, Moody's rating call shortly after the budget, could set the tone for the local market in 2020.

The credit rating agency Moody's - which is expected to downgrade South African government bonds to "junk" this year - in November warned that there is a *“material risk that the government will not succeed in arresting the deterioration of its finances through a revival in economic growth and fiscal consolidation measures”*.

Even Finance Minister Tito Mboweni is frustrated at the slow pace and lack of urgency required by government to implement structural reform, evident in recent tweets:



⇒ Eskom and other SOE debt levels, a sluggish economy, poor growth, higher unemployment, lack of structural reform, expropriation without compensation, prescribed assets, water shortages, corruption, lack of consequences if any, and a potential downgrade could continue to keep investor sentiment at all-time lows which won't bode well for the local economy, stock market or the rand.

ALTHOUGH BRENTHURST REMAINS COGNISANT OF GLOBAL POLITICS AND INTERNATIONAL RISKS, WE REMAIN CAUTIOUSLY OPTIMISTIC ON SPECIFIC GLOBAL GEOGRAPHIES, THEMES AND SECTORS.

BRENTHURST CONTINUES TO ADVISE A GLOBAL, FLEXIBLE PORTFOLIO INVESTED ACROSS ALL ASSET CLASSES INCLUDING BONDS, CASH AND GLOBAL EQUITIES IN ACCORDANCE WITH INDIVIDUAL RISK PROFILES AND INVESTMENT OBJECTIVES. A STRATEGY WHICH WORKED VERY WELL FOR OUR CLIENTS OVER THE PAST FEW YEARS AND WHICH WE EXPECT WILL CONTINUE TO DO SO.

Please do not hesitate to contact any one of our 13 highly qualified financial advisors at our office countrywide.

TO ASSESS INVESTMENT PORTFOLIOS AND REVIEW ISSUES LIKE RISK TOLERANCE, CONSULT ONE OF BRENTHURST WEALTH QUALIFIED, ACCREDITED FINANCIAL ADVISOR. <https://www.bwm.co.za/about-us/>

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